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IN THE

Supreme Court of the United States

OCTOBER TERM 1936.

ARTHUR G. BOGARDUS,

Petitioner,

against

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioner, Arthur G. Bogardus, respectfully prays for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit to review a decree of that Court, entered March 15, 1937, rehearing denied March 11, 1937, affirming a decision of the United States Board of Tax Appeals.

The majority and dissenting opinions of the Circuit Court of Appeals (majority opinion by Judge Learned Hand, dissenting opinion by Judge Thomas W. Swan) are as yet unreported, but appear at R. 92, 99. The opinion of the Board of Tax Appeals (unreported) appears at R. 21.

STATEMENT

The petitioner did not dispute below, and does not dispute here, the findings of fact by the Board of Tax Appeals.

The relevant facts are:

Petitioner was an employee of Universal Oil Products Company (hereinafter called Universal) (R. 77). On January 6, 1931, all of the stock of Universal was sold to United Gasoline Corporation (R. 17). Prior to the sale, the stockholders of Universal had formed an investment company under the name of Unopco Corporation to hold $4,000,000 of current assets withdrawn from the treasury of Universal (R. 17). Unopco had no other purpose and did not either in form or in substance continue the business of Universal, which was the developing and licensing of patents (R. 17, 57). Universal continued in business[1], but with new stockholders (R. 17). After the sale of the Universal stock, and when the stockholders no longer had any interest whatsoever in the business of Universal, one of the stockholders (formerly the President of Universal) suggested to the others that it would be a nice and generous thing to make a gift or honorarium to a number of the old employees of Universal (R. 18, 49). This matter had not been thought of until after the Universal stock had been sold (R. 49, 61-2). Pursuant to this suggestion, the directors *and stockholders* of Unopco voted to pay a bonus to certain former employees of Universal in recognition of their valuable and loyal services to Universal in the past (R. 18, 19).

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[1]See *Skelly Oil Company* v. *Universal Oil Products Company,* 293 U. S. 612, and *Root Refining Company* v. *Universal Oil Products Company,* 296 U. S. 626.

It is stipulated that neither Universal, nor Unopco, nor any of the stockholders of either, were under "any legal *or other* obligation" to make the payments in question (R. 64, 65). It was further stipulated that none of the recipients was or ever had been employed by, or had ever rendered any services to, Unopco or any of its stockholders (R. 63). Again, it was stipulated that the payments were not made or intended to be made by Unopco or by any of its stockholders as payment or compensation for any services rendered or to be rendered, or for any consideration given or to be given to Unopco or to any of its stockholders (R. 65). In fact, the employees had not merely been paid their full salaries for 1930 by Universal, but had in addition been paid bonuses for that year by Universal, in amounts not merely proportionate to their salaries, but evidently calculated to compensate them in proportion to their abilities (R. 77-82).

Universal had been extraordinarily successful in its business, and the sale of its stock netted $25,000,000, representing what was in effect a windfall to its old stockholders.

The total amount of the distribution by the old stockholders of Universal, through Unopco, to past and present employees of Universal aggregated $607,500 (R. 17, 18).

The recipients included not merely employees of Universal, but a number of persons who had been out of the employ of Universal for many years, patent attorneys and patent experts some of whom had not acted for many years, and the sister of an employee of Universal who had been killed in the explosion of a plant thirteen years before (R. 20, 50, 84).

A number of the letters transmitting the moneys to the beneficiaries were included in the stipulation of facts be-

fore the Board (R. 67-76), and they uniformly used language appropriate to gifts, of which the following is typical:

> "Here is the slice of bacon which the old stockholders of Universal want you to have as a gift from them, and which was saved for you out of the party given on January 6 at Chicago" (R. 67-8).[2]

Again:

> "The enclosed check is sent you on behalf of all the old stockholders of Universal as a gift to you in appreciation of the relationship which has existed, and because you were considered one of the family this piece of cake has been saved for you from the party we gave here January 6" (R. 68-9).

Neither Unopco (from whose treasury the gifts were made), nor Universal, nor any of the stockholders, claimed a deduction on their income tax returns (R. 20). Petitioner did not return the gift as taxable income (R. 67).

Accepting as we do the findings of fact by the Board, and the record being undisputed, the function of the Court becomes one to decide whether the correct rule of law was applied to the facts found. *Helvering* v. *Rankin,* 295 U. S. 123, 131, and cases cited; *cf. General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200. The decision of the Board is of course not final on the ultimate question of law whether, on the facts as found, the payment was a compensation or a gift within the statute.

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[2]This refers to the closing of the sale of stock for $25,000,000.00.

APPLICABLE STATUTE

The case is controlled by § 22 of the Revenue Act of 1928 (45 Stat. 797-8). The pertinent provisions follow:

"SEC. 22. GROSS INCOME.

"(a) *General definition.*—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

"(b) *Exclusions from gross income.*—The following items shall not be included in gross income and shall be exempt from taxation under this title:

* * * * * * * *

(3) *Gifts, Bequests, and Devises.*—The value of property acquired by gift, bequest, devise, or inheritance (but the income from such property shall be included in gross income);"

THE QUESTION PRESENTED

The question presented is whether these payments were "compensation" under § 22(a) or "property acquired by gift" under § 22(b)(3).

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

A direct conflict is presented with the decision of the Circuit Court of Appeals for the Third Circuit in *Jones* v. *Commissioner of Internal Revenue,* 31 F. (2d) 755. The same Circuit Court of Appeals adhered to its view in the later case of *Cunningham* v. *Commissioner,* 67 F. (2d) 205.

The case is further indistinguishable in substance from a case in the Ninth Circuit, *Blair* v. *Rosseter,* 33 F. (2d) 286, decided favorably to the taxpayer.

A case involving substantially identical facts with the present case was, however, decided adversely to the taxpayer by the Circuit Court of Appeals for the First Circuit in *Walker* v. *Commissioner* (as yet unreported) decided February 12, 1937, Judge Morton dissenting.[3] A petition for rehearing in this case had not been acted upon at the date of this petition for certiorari.

There appear, therefore, to be three direct decisions in two Circuit Courts of Appeal on this question favorable to the taxpayer, and two decisions in two Circuit Courts of Appeal adverse to the taxpayer. In each of the adverse decisions, one judge dissented (Judge Morton in the *Walker* case in the First Circuit, and Judge Swan in the instant case in the Second Circuit).

Cases involving the same subject (payments by corporations to persons who had rendered services) have arisen in the Fourth, Fifth, and Sixth Circuit Courts of

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[3]**Ten pamphlet copies of the majority and minority opinions in the Circuit Court of Appeals for the First Circuit will be filed herewith.**

Appeal, and in the Court of Appeals of the District of Columbia. Decided in favor of the Commissioner under the particular facts presented:

Noel v. *Parrott* (C. C. A. 4), 15 F. (2d) 669;
Bass v. *Hawley* (C. C. A. 5), 62 F. (2d) 721;
Levey v. *Helvering* (App. D. C.), 68 F. (2d) 401.

Decided in favor of the taxpayer under the particular facts presented:

Lunsford v. *Commissioner* (C. C. A. 6), 67 F. (2d) 740.

The foregoing eight cases arising in seven different Courts of Appeal (together with other cases on the same subject arising in the same courts, *Fisher* v. *Commissioner,* 59 F. (2d) 192 (C. C. A. 2), *Botchford* v. *Commissioner,* 81 F. (2d) 914 (C. C. A. 9), *Lougee* v. *Commissioner,* 63 F. (2d) 112 (C. C. A. 1), *Anderson* v. *Commissioner,* 79 F. (2d) 979 (C. C. A. 2), *Davis* v. *Commissioner,* 81 F. (2d) 137 (C. C. A. 6), and *Weagant* v. *Bowers,* 57 F. (2d) 679 (C. C. A. 2)) indicate the constant recurrence of the question and the importance and desirability of an authoritative decision thereon by this Court, quite apart from the fact that on the facts of this case (as compared with the facts in *Jones* v. *Commissioner,* 31 F. (2d) 755, *supra*), a clear-cut conflict is presented.

The present case presents an apt opportunity for such an authoritative decision, in that all of the indiciae in the record, and as found by the Board, are in favor of the taxpayer's view, except only that the language of the Unopco

Corporation resolution included a reference to "recognition" by the former stockholders that "valuable and loyal services" had been rendered to Universal, the corporation in which they no longer had any interest.

Accordingly, the case presents the broad question whether the single fact of recognition, in the mind of the donor[4], is conclusive against the taxpayer. Stated conversely, the question is presented whether, in order to constitute a gift under the statute, the payment must be (as a majority of the Court below indicated it must be) "an unconstrained act of affection or regard".

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Court, directed to the United States Circuit Court of Appeals for the Second Judicial Circuit, sitting at New York, New York, commanding said Court to certify and send up to this Court, on a date to be designated, a full and complete transcript of the record and of all proceedings in the Circuit Court of Appeals had in this case, to the end that this case may be reviewed and determined by this Court; that the decree of the Circuit Court of Appeals be

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[4]The Circuit Courts of Appeal, following a decision by the Second Circuit in *Fisher* v. *Commissioner*, 59 F. (2d) 192, have generally agreed that the intent of the donor is the governing consideration. As pointed out in Judge Swan's dissenting opinion, the Board made no ultimate finding in the present case that the stockholders had a compensatory and not a donative interest, but left to the Court the question (one of law) whether, on the facts *as found*, the payment represented compensation or a gift.

reversed; and that your petitioner be granted such other and further relief as may seem proper.

ARTHUR G. BOGARDUS,
Petitioner

By

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Counsel for Petitioner,
Office & Post Office Address,
15 Broad Street,
New York, N. Y.

March 19, 1937.

BRIEF IN SUPPORT OF PETITION

OPINIONS BELOW

The majority and dissenting opinions of the Circuit Court of Appeals (majority opinion by Judge Learned Hand, dissenting opinion by Judge Thomas W. Swan) are as yet unreported, but appear at R. 92, 99. The opinion of the Board of Tax Appeals (unreported) appears at R. 21.

JURISDICTION

The jurisdiction of this Court is invoked under § 240(a) of the Judicial Code as amended by the Act of February 13, 1925 (43 Stat. 938, 28 U. S. C. § 347(a), and § 1003(a) of the Revenue Act of 1926 (44 Stat. 110, 26 U. S. C. § 1226(a)). The date of the decree of the Circuit Court of Appeals for the Second Circuit to be reviewed was March 15, 1937. Rehearing was denied March 11, 1937.

SPECIFICATION OF ERRORS

(1) The Court below erred in affirming the decision of the Board of Tax Appeals, decreeing that there was a deficiency due by the petitioner in respect of his income tax for the calendar year 1931.[5]

(2) The Court below erred in holding that the same payments "may be at once *'gifts'* under § 22 subdivision (b)(3), and *'compensation for personal service'* under subdivision (a)".

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[5]The deficiency in this particular case is a very small amount, but the *principle* of this case governs those of the other recipients of the same benefaction and the aggregate amount involved is substantial.

(3) The Court below erred in holding that the payments here involved, "though gifts", were taxable.

(4) The Court below erred in confining gifts in effect only to those which resulted solely because the relation of employee to employer "had bound them in a warm friendship", and in rejecting as gifts all those where there exists "something which makes the payment more than an unconstrained act of affection or regard".

(5) The Court below erred in holding that the proposal to make a "gift or honorarium" evidenced an intent to pay compensation, because the word "honorarium" is "a word never used except to denote a compensatory payment; * * *"[6]

(6) The Court erred in holding that the intent and motive of the donors "was precisely the same as though the shareholders had been the employers of the donees, *which they were not.*"

STATEMENT AND ARGUMENT

The facts are stated in the petition for the writ. There is no dispute as to the facts, for we accept the findings of the Board, and the record otherwise consists principally of a stipulation, and partially of uncontradicted testimony.

The error is one of law.

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[6]The Court's opinion refers only to "honorarium", but the word "gift" is coupled with it in the record (R. 18, 49). In any event, there is an explicit controversy with the Third Circuit over the meaning of "honorarium", that Court saying in *Cunningham* v. *Commissioner,* 67 F. (2d) 205, *supra:* "It is clear to us that the money was a gift, a voluntary honorarium, * * *."

The Circuit Court of Appeals frankly says that it considers that there is a class of taxable gifts. This appears to us to be little else then judicial legislation, as Congress selected its own terminology and decreed that "gifts" should not be taxable.

Old Colony Trust Company v. *Commissioner,* 279 U. S. 716, does not aid the Court below. The Court below construed it as holding that payments may be *both* gifts and compensation, *i.e.,* construed it as an instruction to the Courts to disregard the terminology of the statute (which made the question whether the payments were gifts or compensation determinative of the question of taxability). We find no such meaning in the opinion of this Court. What this Court did hold was that a payment might under certain circumstances be a gift, even though not made pursuant to a *legal obligation.* The relevant language (279 U. S. at pp. 729 and 730) follows:

> "The certificate shows that the taxes were imposed upon the employee, that the taxes were actually paid by the employer and that the employee entered upon his duties in the years in question under the express agreement that his income taxes would be paid by his employer. This is evidenced by the terms of the resolution passed August 3, 1916, more than one year prior to the year in which the taxes were imposed. The taxes were paid upon a valuable consideration, namely, the services rendered by the employee and as part of the compensation therefor. We think therefore that the payment constituted income to the employee."
>
> * * * * * * * *
>
> "Nor can it be argued that the payment of the tax in No. 130 was a gift. The payment for services,

> even though entirely voluntary, was nevertheless compensation within the statute * * *."

In the *Old Colony* case, the taxpayer apparently argued that, because there was no *legal* obligation, it necessarily followed that the payment was a gift. The holding of this Court went no further than to negative this and to state that where there was consideration for the payment, the lack of a legal obligation would not convert it into a gift.

But in the present case, on the other hand, there was not merely no legal obligation, but there was *no* "other obligation" (R. 64, 65). The payment, moreover, "was not made or intended to be made * * * for any consideration" moving to the donor (R. 65). Moreover, no detriment, such as loss of employment, was suffered by the recipients. The payment was one purely of "spontaneous generosity".

In this case are combined all of the indiciae which have been formerly recognized by Circuit Courts of Appeal in employer-employee cases, as evidencing intention to make a gift:

> 1. The recipients had never been employed by Unopco, the donor, or by its stockholders, and had never rendered any services to them (R. 63).
>
> 2. Unopco, and its stockholders, had *no interest whatsoever* in the future services of the recipients, who continued in the employ of Universal (R. 56).
>
> 3. The distribution by the old Universal stockholders through Unopco had not even been thought of until all relationship with Universal and its employees had been severed (R. 49, 61-2).

4. The distribution was termed a "gift" in contemporary statements and correspondence (R. 18, 67-76).

5. The distribution was approved as a gift by the stockholders of Unopco, evidencing that it was not deemed within the powers of the Board of Directors to grant (R. 18).

6. No deduction, either by Universal, by Unopco, or by the individual shareholders, was taken for this distribution as compensation paid employees (R. 20).

7. Unopco, the donor, and its stockholders were under no "legal or other obligation" to make this payment (R. 64, 65).

8. The payment was "not made or intended to be made * * * as payment or compensation for any services rendered or to be rendered or for any consideration given or to be given * * * to said Unopco Corporation or to any of its stockholders" (R. 65).

It is respectfully submitted that, if the Commissioner is to prevail in the present case, then there will be no case in which a former employee will ever be construed to receive a gift except only that case in which the employment has served merely as the medium for introducing the employer to the employee, and the gift has flown exclusively from a relationship of love or affection thereafter arising on personal grounds between them. Indeed, this is the view of the majority of the Circuit Court of Appeals. The single fact that the donor had some *recognition* that valuable and loyal services had been rendered in the past

(as distinct from having mere love or affection) was held decisive. In effect, gifts are by this decision confined to relatives or persons occupying analogous positions.[7]

The following were the facts in the cases which reached a contrary result:

Jones v. *Commissioner* (C. C. A. 3), 31 F. (2d) 755.

This case provides the clear-cut conflict with the present one. The stockholders of a corporation sold their stock to third parties for $3,000,000. $300,000 of this amount was by previous agreement distributed to the officers and administrative staff of the corporation, who had been long employed by it, since it was felt that they would lose their positions by reason of change of ownership. The corporation had considered making this payment to its employees, but later the plan was changed since it was felt the corporation could not legally make a gift. The officer in charge referred to the desirability of making the payment "in consideration of such a sudden termination of the business association and in recognition of the efforts and devotion of the officers and certain old employees of the companies over a long period of years." (10 B. T. A. 202, 204). The Circuit Court of Appeals stated that the payment was "in recognition of the past faithful work of the staff" (31 F. (2d) at p. 756).

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[7]That no case could be stronger for the taxpayer than the present is illustrated with peculiar aptness by the fact that the letters of the President to recipients, which letters were in effect part of the *res gestae*, said that the gifts were being made because the recipients were recognized as "one of the family" (R. 69, 70), or as "a member of the family" (R. 72, 76).

The case was a distinctly stronger one for the Commissioner than the present case, in that (1) the officers and old employees there suffered the detriment of losing their positions (whereas in our case those who had not previously terminated their employment, continued in the employ of Universal), and (2) the employer had itself considered making the payment (whereas in our case the suggestion that the payment be made never arose until after all relationship had been severed between the corporate employer and the paying shareholders).

In the *Jones* case the Board of Tax Appeals, as in our case, had decided in favor of the Commissioner. This decision was *reversed* by the Circuit Court of Appeals. The decision of the Circuit Court of Appeals for the Third Circuit is therefore directly in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in this case, which affirmed the Board of Tax Appeals.

Cunningham v. *Commissioner* (C. C. A. 3), 67 F. (2d) 205

This case confirmed the view enunciated by the Circuit Court of Appeals for the Third Circuit in *Jones* v. *Commissioner, supra.* Here the stock of a corporation had been purchased by Canadian interests and a new set of directors elected. The president voluntarily resigned. Thereupon, the Board of Directors made a payment of $15,000 to the president "in appreciation of Mr. Cunningham's excellent guidance of this corporation during the times of difficulty and depression". The Board of Tax Appeals held for the Commissioner and decided that the payment was compensation. The Circuit Court of Appeals for the Third Circuit reversed the Board of Tax Appeals

and held that the payment was a gift, thus conflicting in theory with the decision of the Circuit Court of Appeals for the Second Circuit in the instant case.

By reversing the Board of Tax Appeals in the *Jones* and *Cunningham* cases, *supra*, the Circuit Court of Appeals for the Third Circuit necessarily held that there was no substantial evidence supporting the decision of the Board that the payments were compensation, and hence these decisions are in direct conflict with the instant case in so far as it may hold that the Board's decision was supported by substantial evidence and could not be reversed.

Blair v. *Rosseter* (C. C. A. 9), 33 F. (2d) 286.

In this case a corporation, with full approval of its stockholders, made a payment of $50,000 to its president "as a gift in recognition of his able and successful direction of the affairs of the company through the past ten years". The Court defined a gift as a "voluntary transfer of property from one to another without any consideration or compensation therefor", and held that the payment to the president was a gift and not compensation for services.

Lunsford v. *Commissioner* (C. C. A. 6), 67 F. (2d) 740.

Here a corporation made a payment of $50,000 to an employee of another corporation (but with the assent of the employing corporation) for his services in putting through a sale of assets by the paying corporation to the employing corporation. Although it did not appear that the stockholders of the paying corporation had ratified the payment, the Court held that it was a gift.

It therefore appears that not only is the decision of the Circuit Court of Appeals for the Second Circuit in the instant case on a matter of substantial importance, but it is in conflict with decisions in other Circuits.

For the foregoing reasons, it is respectfully requested that this Court exercise its supervisory powers and that the writ be allowed.

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